

# CURRENTS

WESTERN CANADA'S  
ECONOMIC BULLETIN

## FEATURE STORY

Social licence critical  
to developing the  
West's resources

CANADA WEST FOUNDATION FEBRUARY 2014



## LOONIE IN A TAILSPIN

What's behind the drop in  
the Canadian dollar?

GLOBAL ECONOMY

## LITTLE HOUSE ON THE PRAIRIE

Immigration boom in the West

BEHIND THE NUMBERS

## BUMPER CROP

Huge harvest in Manitoba  
and Saskatchewan

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## GLOBAL ECONOMY

## A lower Canadian Dollar in 2014

MICHAEL HOLDEN, SENIOR ECONOMIST

The once-mighty loonie has been struggling in recent months. A year ago, it was trading on par with the U.S. dollar. By October it had fallen to about 96.5 cents U.S.. In the last couple of months, however, the decline has accelerated. The exchange rate dipped below 90 cents U.S. in January – its lowest point since August 2009.

There are a number of factors driving the dollar lower. First, the weakening loonie reflects, in part at least, a general strengthening of the U.S. dollar as economic conditions improve south of the border. The U.S. dollar is making gains, not just against the loonie, but against other major currencies as well.

Second is softening global commodity prices. Since the early 2000s, fluctuations in the Canadian dollar have mirrored movements in commodity prices, and the price of crude oil in particular. Slower growth in China, among other factors, has contributed to lower prices for energy and metals since the summer, pushing the Canadian dollar down along with it.

Another factor behind the falling loonie has been a not-so-subtle signalling effect from the Bank of Canada. Among its core functions, the bank works to keep inflation low, stable and predictable. Current policy is to keep inflation near 2% (within a 1% to 3% band). However, inflation has been at or below the bottom of that range throughout 2013.

Weak inflation has been attributed to stiffening competition in the retail sector driving down prices of consumer goods – the so-called “Target effect” – as well as persistently slack output levels, which is the result of prolonged weakness in non-crude-oil exports.

Under normal circumstances, the Bank of Canada would respond to falling inflation by cutting interest rates. Doing so makes it cheaper to borrow money, sparking investment, economic growth and, eventually, inflation. The problem is that interest rates are already about as low as they can get. The bank’s trendsetting interest rate is 1%, where it has sat for nearly three and a half years.



The dilemma the bank faces is that these persistent low rates have created a consumer debt problem. Low interest rates have made it relatively cheap for Canadians to take on large mortgages, lines of credit and credit card balances. The concern is that when rates rise, the cost of holding all that debt becomes much more onerous. From the bank’s perspective, lowering interest rates even further in the short term would only encourage more borrowing and exacerbate the problem.

This is where the Canadian dollar comes in. The Bank of Canada does not explicitly manipulate the exchange rate, but it certainly can influence its movements. In its January *Monetary Policy Report*, the bank made a number of veiled hints about the future direction of interest rates and the Canadian economy generally that had the effect of pushing the dollar down even further.

By so doing, the bank accomplishes its goals without touching interest rates. A lower dollar will raise the cost of imported goods, like bananas or flat-screen TVs. This puts upward pressure on inflation. A weaker loonie will also help boost exports because a lower dollar means that Canadian products are more competitively priced in global markets.

While many exporters are happy at the prospect of a lower dollar, the benefits are likely to be less pronounced in the West. To be sure, many western Canadian exporters will welcome this development. So too will our tourism operators.

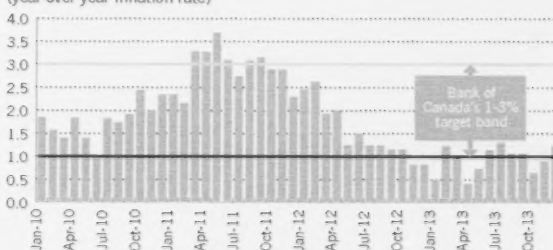
However, much of western Canada’s export base centres on commodities trade. For commodities exporters, especially those selling crude oil and minerals, movements in the exchange rate do not matter as much as they might for manufacturers or other exporters. Since commodity prices usually move in the same direction as the exchange rate, a lower dollar is of small benefit to oil producers, for example, if it is accompanied by weaker oil prices.

## THE CANADIAN DOLLAR TRACKS COMMODITY PRICES

Index: 1972=100



Source: Bank of Canada, Statistics Canada, Canada West Foundation

INFLATION IS AT THE BOTTOM END OF THE TARGET BAND  
(year-over-year inflation rate)

Source: Bank of Canada, Canada West Foundation

## WESTERN COMMENTARY



## Social licence issues critical to resource development in the West

LEN COAD, DIRECTOR – CENTRE FOR NATURAL RESOURCES POLICY

Alberta and British Columbia recently released a joint task force report on how the two provinces can work together to deliver energy to global markets. It serves as yet another reminder of how critical social licence is to future resource development in the West.

The task force team consisted of five working groups: responsible development and public engagement, marine and terrestrial spillage, First Nations, transportation, and fiscal and economic benefits. Its report clearly recognizes that these themes are interconnected. For example, responsible development requires an approach to preventing and mitigating marine and terrestrial spills, as well as First Nations consultation (if applicable). The public must have confidence that these issues are being properly managed.

The report also notes that there is “a disconnect between public perception and the reality of the Canadian oil and gas sector’s contribution to jobs, personal income, the economy, and energy security for Canadians...”<sup>1</sup> The task force proposes actions to address the disconnect.

It is critically important that these issues are addressed. Western Canada’s natural provincial economies depend heavily on their ability to develop, produce, and market resources. Canada’s resource industries derive a large share of their revenues from their operations in the four western provinces (see charts). In turn, society’s support for resource development depends on the five themes addressed by the task force.

Social licence has both local and global dimensions. It begins, however, at the community level. Those most affected by resource development must have confidence that the resulting economic benefits are fairly and equitably distributed. Companies must also be comfortable that they can deliver the benefits they promise. Communities, governments and companies must work together to ensure that the natural environment, community health, individual health and safety are protected and enhanced. Where Aboriginal communities are involved, their unique standards of engagement, communications and cultural support must be respected. The trust that comes from delivering on these issues is the core of social licence.

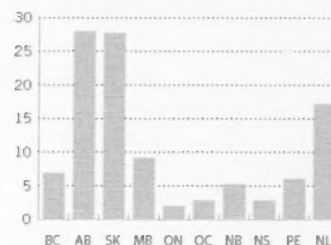
The increasingly northern dimension of western Canada’s resource development adds further challenges. Northern communities often lack the community-level infrastructure – such as roads, schools, health facilities and recreational centres – to accommodate the rapid, and sometimes temporary, growth that accompanies resource projects. In addition, local residents may not have the skills, training or education to take full advantage of the opportunities that resource projects present. Such issues are usually addressed through arrangements for sharing the benefits of the project with local communities, but sometimes they are too complex for companies and communities to resolve on their own. In these cases, provincial support is essential to success. Delivering on the themes identified in the task force report will provide confidence that the provinces are willing to participate.

Broader issues are also acting as social licence demerits. The lack of progress, particularly in Alberta, on reducing GHG emissions has undermined support for the pipeline infrastructure that would carry bitumen to market. Climate change activists are increasingly voicing their opposition. This issue was out of scope for the task force, but it is clearly part of the broader social licence debate. Hopefully the more narrowly focused cooperation outlined in the task force will provide a framework and common experience to tackle additional issues.

### RESOURCE EXTRACTIONS IMPACT ON EACH PROVINCE

#### RESOURCES MATTER TO THE WEST

(resource extraction as a % of GDP)



Source: Statistics Canada, Canada West Foundation

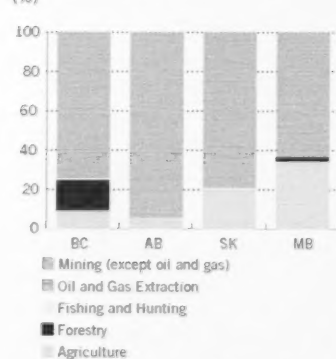
Resource industries  
directly account  
for nearly

**20%**

of economic activity  
in the West.

Source: Canada West Foundation

#### SHARES OF RESOURCE SECTOR GDP BY PROVINCE



Source: Statistics Canada, Canada West Foundation

<sup>1</sup> British Columbia/Alberta Deputy Ministers Working Group, p. 4.

## BRITISH COLUMBIA



## Waiting for the sun to shine

It will take many months before all the numbers come in, but indications are that 2013 was another middling year for the B.C. economy. Provincial GDP expanded by about 1.5% in 2012 and most economists believe that growth was even slower in 2013.

The most obvious evidence of B.C.'s struggles has been in provincial labour markets. In spite of a strong monthly performance in December, which saw the province add 12,800 jobs, overall employment in 2013 fell by 0.2% compared to 2012 levels. Only Nova Scotia posted worse job-creation numbers last year.

Weak labour markets have also meant stagnant wage growth in B.C.. Average weekly earnings in the province have been essentially unchanged for an entire year. In October 2013, average weekly earnings in the province were \$878, compared to \$877 in November 2012. British Columbians' purchasing power remained unchanged last year. Inflation in the province dipped into negative territory in 2013.

The economic news coming out of B.C. is not all dire. In particular, the province's housing market appears to be roaring back to life. Home sales were up considerably in the second half of 2013 and average resale prices have risen by 8.5% since June. The average cost of a home in B.C. is back to near-record levels.

The one bit of bad news in real estate is that the number of unfilled new homes in Vancouver has risen sharply and is sitting at its highest level since the mid-1990s. This surplus capacity in B.C.'s largest real estate market is bound to put some downward pressure on housing prices in 2014.

Provincial finances in B.C. appear to be on solid footing. Income tax and resource revenues are down through the first half of the 2013-2014 fiscal year, but these were offset by stronger corporate taxes and higher-than-expected income from the Insurance Corporation of British Columbia. As a result, the province remains on track to deliver a small surplus this year.

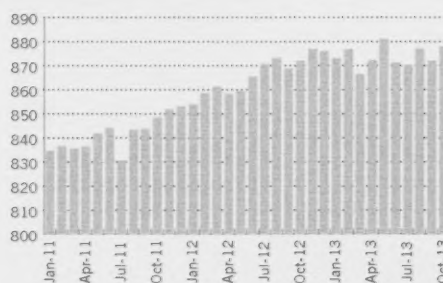
Looking ahead, there is reason to be optimistic that 2014 will be a better year in B.C.. Exports have been one of the province's bright spots and a recovering U.S. economy, a lower Canadian dollar and strengthening lumber prices should all contribute to an even better performance next year. In addition, preliminary work may get underway later in the year on developing some of the LNG projects that have been proposed. If and when those projects begin, they will point the way to stronger economic growth in B.C. over the next several years.



B.C.'s inflation rate in 2013 was  
**-0.1%.**

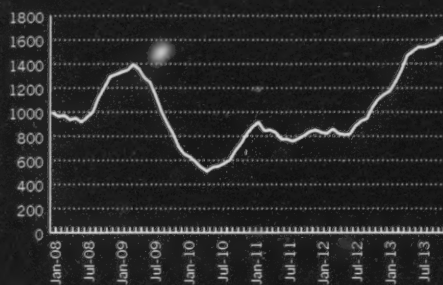
Source: Statistics Canada

### WAGES IN B.C. HAVE FLATTENED OUT (average weekly earnings in \$)



Source: Statistics Canada

### UNSOLD NEW HOMES IN VANCOUVER (Units)



Source: Statistics Canada

## ALBERTA

## An object in motion tends to stay in motion

The Alberta economy is rolling along. In spite of the flooding in June, 2013 was another strong year. A surging population, solid business investment and good macroeconomic conditions point to even higher expectations for 2014.

However, Alberta will be challenged this year to generate enough jobs to absorb all the newcomers to the province. In spite of a dip in December, total employment was up 2.8% for 2013, a strong showing but not enough to offset the influx of new residents; the working-age population grew by 3.3% last year. The only reason the unemployment rate remained stable is because there was a drop in the number of Albertans looking for work in 2013.

After stalling in the summer, wage growth has picked up again in Alberta. Average weekly earnings rose by 2.0% from July to October, thanks in part to a surge in employment in the high-paying oil and gas sector. Earnings in Alberta are nearly 23% higher than the national average – the widest gap on record.

Alberta has the strongest consumer markets in Canada. A combination of population growth, job creation and high wages has kept residents in a shopping mood. Retail sales in the province through October are up 6.5% compared to the same period in 2012 – well over twice the national average.

Businesses in Alberta also appear confident heading into 2014. Business investment hit a new record of almost \$88 billion last year, buoyed by a substantial increase in purchases of new machinery and equipment in the industrial sector. More than half of last year's total investment took place in the oil and gas sector.

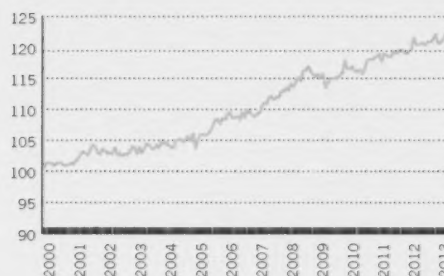
On a related note, investment in non-residential construction was up in 2013 and accelerated as the year went on – good news for construction activity in 2014. The one weak spot in the province is Edmonton, where non-residential construction has been on a downward trend for the past three years. This is likely to change when ground breaks on the new downtown arena project.

The provincial government is also doing better than expected as Albertans round the corner towards the 2014 budget. Through the first half of the fiscal year, the province produced an operating surplus of \$1.1 billion, compared to budget expectations of a small deficit. The surplus to date comes in spite of \$443 million in unforeseen disaster/emergency assistance spending. Higher bitumen royalties (\$1.2 billion above expectations) and lower health care spending (\$507 million below expectations) are largely responsible for the improved fiscal outlook.



### ALBERTA'S WAGE ADVANTAGE IS WIDENING

(average weekly earnings in Alberta as a % of the national average)



Source: Statistics Canada, Canada West Foundation

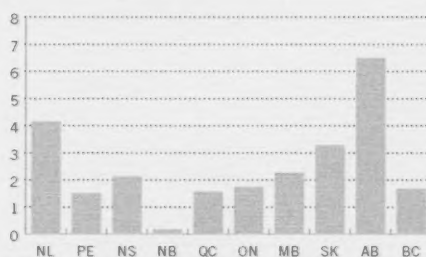
### Industrial sector investment in machinery and equipment was up

# 11.9% in 2013.

Source: Statistics Canada

### CONSUMER MARKETS REMAIN HOT

(% retail sales growth, Jan-Nov 2013)



Source: Statistics Canada

## SASKATCHEWAN

### A strong year will be hard to repeat

Buoyed by robust labour markets and an excellent crop year, Saskatchewan is coming off a strong economic performance in 2013. The only significant negative last year was in potash markets, where the collapse of a Russian/Belorussian cartel is creating ongoing price and production uncertainty in Saskatchewan.

Agriculture and potash are also tempering expectations for the Saskatchewan economy in 2014. Saskatchewan is unlikely to build on last year's excellent harvest, meaning that agriculture will not drive additional growth. Similarly, potash production in 2013 was strong before the cartel dissolution (up 11.5% through September), but growth this year is almost certain to be lower.

What this boils down to is that Saskatchewan is unlikely to sustain last year's success. The province edged out Alberta to post the strongest labour market performance in Canada in 2013. Overall employment grew by 3.4%, pushing the annual unemployment rate down to 4.0% - the lowest rate of any province. The only cause for concern is that these gains all came in the first half of the year. Job growth has been flat since July.

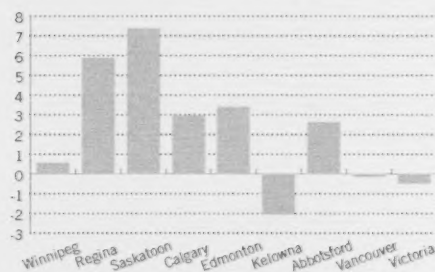
Labour market gains in 2013 were heavily concentrated in the twin engines of Saskatoon and Regina. The number of jobs in Saskatoon jumped by a remarkable 7.4% last year, by far the best job-creation record of any major city in western Canada and second best performance nationally, behind Barrie, Ont. Regina was next, with 5.9% employment growth in 2013. Saskatoon and Regina also have by far the lowest municipal unemployment rates of any major city in Canada.

As mentioned above, Saskatchewan enjoyed a bumper crop in 2013. Production of wheat, canola and barley - the province's three most important field crops - were up significantly compared to 2012 levels. The wheat and barley harvest was up by 44%, while canola seed volumes were 37% higher.

One potential cause for concern in 2014 is that the province's fiscal surplus may be at risk. In the 2013 budget, the province projected a \$32.4-million surplus in its General Revenue Fund, but six months into the fiscal year, that figure has shrunk to \$11.4 million. The main factors behind this decline are lower potash royalties and sales tax revenues which are weaker than expected, given the province's job numbers and wage growth. Fortunately for the province, oil revenues have been strong because of a combination of higher world crude prices and a narrower price differential for western Canadian crude in the first half of the year. However, that gap has recently been widening again, creating additional risk for the provincial government.



**EMPLOYMENT GROWTH BY MAJOR CITY IN WESTERN CANADA**  
(2013 employment growth by major city in the West %)



Source: Statistics Canada

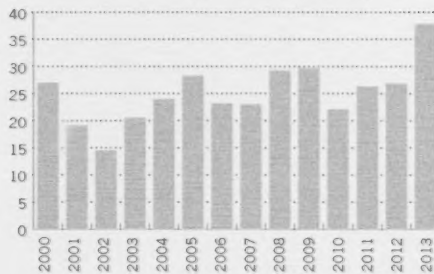
**Saskatoon's unemployment rate in 2013 was**

**3.7%**

**– the lowest of any major city in Canada.**

Source: Statistics Canada

**BUMPER CROPS IN SASKATCHEWAN**  
(production of major crops, in millions of tonnes)



Note: Includes wheat, canola, barley, oats, peas, lentils and flaxseed.

Source: Statistics Canada, Canada West Foundation

## MANITOBA



### Bumper fall harvest slow in reaching markets

Manitoba's recent economic performance has been a mixed bag. Pockets of strength are helping to keep the economy growing, but there are significant weak spots in the province as well. Fortunately, external conditions are improving, meaning that we can expect some improvement in these areas this year.

On the positive side, like Saskatchewan, Manitoba enjoyed a bumper crop in 2013 for all its major field grains and oilseeds. Wheat production was up 32% over 2012 levels, while canola was 37% higher. Corn, the province's third-largest crop, was 51% higher. This boom is excellent news for farmers – cash receipts for grain farmers are up 29% through the first three quarters of 2013.

This harvest is also helping to pad Manitoba's 2013 export statistics. Through November, Manitoba has seen the fastest growth in exports of any province (10.5%), buoyed by a surge in wheat sales late in the year. Exports of soybeans, crude oil, electricity and agricultural machinery are also higher.

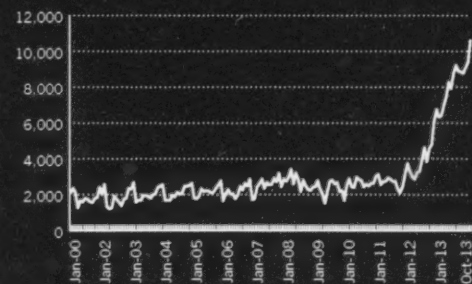
In spite of the surge in wheat exports, a major challenge resulting from the 2013 harvest is that there is not enough rail capacity in place to get all that grain to market. Some estimates suggest that grain shipments to export terminals are as much as two months behind schedule, costing the economy millions of dollars in late fees at ports. Rail companies are doing their best to accommodate the surge in demand, but are facing accusations that they are giving preferential treatment to crude oil shipments. Although crude oil represents just a small fraction of total rail traffic in western Canada, it is rising quickly. In October 2013, railway companies in the West loaded 10,600 cars with crude oil and fuel oil, a 65% increase compared to just a year earlier.

Manitoba's labour markets had a poor showing in 2013, but this can almost entirely be pinned on a hangover effect in construction. Overall employment last year grew by just 0.6% (about 3,800 jobs). However, that growth came in spite of 12,100 fewer jobs in construction from February to December as work on major projects in the province wound down. With that hangover effect mostly out of the way, employment growth should rebound.

Manufacturing in the province remains weak as the final 2013 numbers trickle in. Through November, manufacturers' sales are down 0.5% compared to the same period in the previous year – the weakest performance in western Canada. The good news is that a decline in the Canadian dollar and evidence of an economic resurgence in the U.S. point to better times ahead in this year.

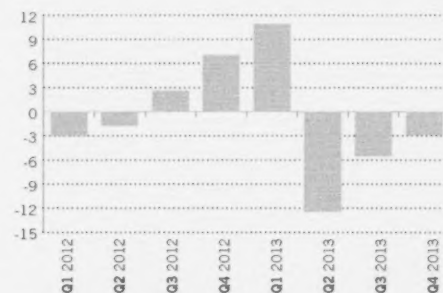


**CRUDE OIL SHIPMENTS ARE FILLING RAIL CAPACITY**  
(Number of rail cars loaded with oil in western Canada)



Source: Statistics Canada

**CONSTRUCTION EMPLOYMENT HANGOVER**  
(quarterly growth in construction jobs %)



Source: Statistics Canada, Canada West Foundation

**12,000**  
fewer construction jobs in  
December compared to February.

Source: Statistics Canada

## BEHIND THE NUMBERS

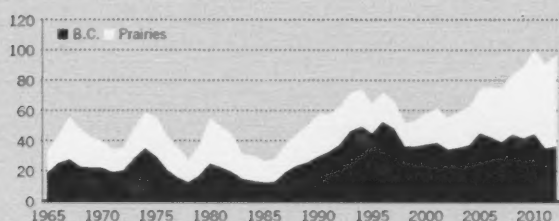
### B.C. is no longer western Canada's most popular immigrant destination, as a wave of new Canadians settle on the Prairies.

Western Canada is enjoying an immigration boom. In 2012, 97,000 immigrants settled in the West, up from 55,000 10 years earlier. Nearly 38% of all immigrants to Canada initially settle in the West.

Remarkably, virtually all this growth is coming on the Prairies. B.C. has long been by far the most popular destination in the West for newcomers to Canada. In the mid-late 1990s, 70% of all immigrants to the West went to B.C.. Since the early 2000s, however, immigration to B.C. has been stagnant, while it is taking off on the Prairies. More immigrants now settle in Alberta than in B.C..

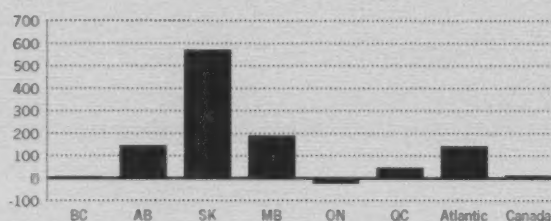
Even so, Alberta is not where the most dramatic growth in immigration has been. Over the last 10 years, immigration to Saskatchewan has increased by 570%, albeit from a very low base. In spite of the growth, Saskatchewan still attracts the fewest immigrants of any western province. Immigration growth in Manitoba and Alberta since 2002 has been 188% and 144%, respectively. In B.C., immigration is up just 6.4%.

**IMMIGRATION BOOM IN THE WEST**  
Number of new immigrants (000s)



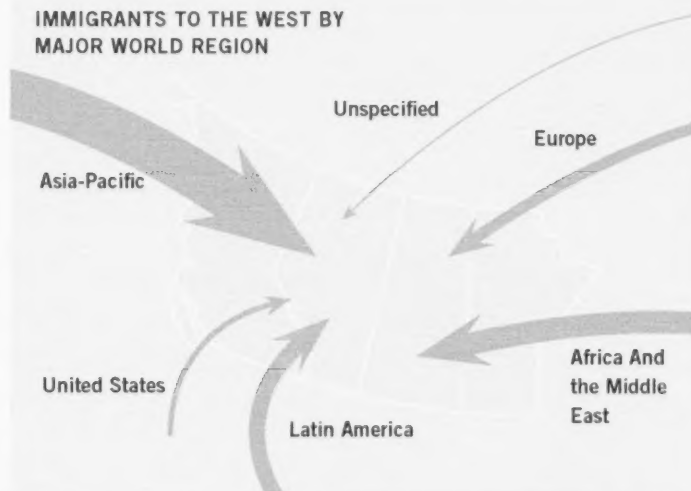
Source: Statistics Canada

**GROWTH IN IMMIGRATION SINCE 2002**  
(%)



Source: Canada West Foundation calculations using Statistics Canada data

### IMMIGRANTS TO THE WEST BY MAJOR WORLD REGION



|                            | NUMBER | SHARE OF TOTAL | % GROWTH IN PAST 5 YEARS |
|----------------------------|--------|----------------|--------------------------|
| Africa and the Middle East | 13,257 | 13.7           | 43                       |
| Asia-Pacific               | 63,842 | 65.9           | 41                       |
| Latin America              | 10,588 | 10.9           | -8                       |
| United States              | 3,598  | 3.7            | -8                       |
| Europe                     | 5,511  | 5.7            | 29                       |
| Unspecified                | 26     | 0.03           | -38                      |

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